

GAO

Report to the Chairman, Subcommittee  
on Social Security, Committee on Ways  
and Means, House of Representatives

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August 2002

# SOCIAL SECURITY ADMINISTRATION

## Revision to the Government Pension Offset Exemption Should Be Considered



G A O

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## Abbreviations

CSRS	Civil Service Retirement System
FERS	Federal Employees Retirement System
GPO	Government Pension Offset
SSA	Social Security Administration



United States General Accounting Office  
Washington, DC 20548

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August 15, 2002

The Honorable E. Clay Shaw  
Chairman  
Subcommittee on Social Security  
Committee on Ways and Means  
House of Representatives

Dear Mr. Chairman:

This report addresses your request for information on the Government Pension Offset (GPO) exemption. Generally, Social Security benefits are payable to the spouses of retired, disabled, or deceased workers covered by Social Security. These benefits often provide income to wives and husbands who have little or no Social Security benefits of their own. If both spouses worked in positions covered by Social Security, each may not receive both the benefits earned as a worker and the full spousal benefit; rather the worker receives the higher amount of the two. However, until 1977, workers receiving pensions from government positions not covered by Social Security could receive their full pension benefit and their full Social Security spousal benefits as if they were nonworking spouses. At that time, legislation was enacted<sup>1</sup> creating a GPO, to equalize the treatment of workers covered by Social Security and those with noncovered government pensions. The GPO prevented workers from receiving a full spousal benefit on top of a pension earned from noncovered government employment.<sup>2</sup> However, the law provides an exemption from the GPO if an individual's last day of state/local employment is in a position that is covered by both Social Security and the state/local government's pension system.<sup>3</sup> In these cases, the GPO will not be applied to the Social Security spousal benefit. The intent of the "last-day" exemption is unclear in the legislation.

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<sup>1</sup> Public Law 95-216, Section 334 (1977).

<sup>2</sup> Currently, the reduction in spousal benefits is two-thirds of the amount of their public pension.

<sup>3</sup> Exemption due to "The Last Day of Employment" Covered Under Social Security – State/Local or Military Service Pensions (SSA's Program Operations Manual System, GN 02608.102).

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Specifically, you asked us to (1) assess the extent to which individuals retiring from jobs not covered by Social Security may be transferring briefly to jobs covered by Social Security in order to avoid the GPO, (2) estimate the impact of such transfers on the Social Security Trust Fund, and (3) identify options for addressing potential abuses of the last-day exemption. On July 9, 2002, we briefed your staff on the results of our work. This report formally conveys the final version of the document used at that briefing.

This review originated from a referral to GAO's FraudNET questioning a practice in Texas where individuals were transferring to Social Security-covered positions for one-day to avoid the GPO.<sup>4</sup> To perform our work we first reviewed the GPO's legislative history and government reports documenting the purpose of the offset and the Social Security Administration's (SSA) policies and procedures for administering it. There is no central data on use of the GPO exemption by individuals and time constraints did not permit in-depth audit work on the approximately 2,300 state and local government retirement plans nationwide. Therefore, to assess the extent of these job transfers, we performed limited work with associations, researchers, and retirement system officials in 28 states. We selected these states either because they were authorized to operate retirement systems with both covered and noncovered positions or because their state or local government plans had a mix of covered and noncovered positions, thus offering the greatest potential for use of the last-day exemption. We also interviewed and obtained documentation from SSA headquarters and regional officials; and other federal officials knowledgeable about the subject matter, such as the Congressional Budget Office and the Internal Revenue Service. Finally, we visited and performed audit work in Texas and Georgia, two of the states where we identified use of the last-day exemption. We conducted our work from April through June 2002 in accordance with generally accepted government auditing standards.

Given our time constraints we could not definitively confirm that this practice is occurring in other states. However, we were able to establish that in Texas and Georgia 4,819 individuals as of June 2002 performed work in Social Security covered positions for short periods to qualify for

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<sup>4</sup> FraudNET is a service maintained by GAO's Office of Special Investigations. GAO subsequently determined that use of the GPO last-day exemption is permitted under the law.

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the GPO last-day exemption.<sup>5</sup> Texas officials reported 4,795 individuals; Georgia officials reported an estimated 24 cases. SSA officials also acknowledged that use of the exemption might be possible in some of the approximately 2,300 state and local government retirement plans in other states where such plans contain Social Security covered and noncovered positions. In Texas, teachers typically worked a single day in a nonteaching position covered by Social Security, such as a clerical or janitorial position. Based on an hourly wage of about \$6, these individuals in Texas typically paid a total of \$3 in Social Security taxes. In Georgia, teachers generally agreed to work for approximately one year in another teaching position in a school district covered by Social Security. Officials in both states indicated that use of the exemption would likely continue to grow as awareness increases and it becomes part of individual's retirement planning.

For the cases we identified in Texas and Georgia, increased long-term benefit payments from the Social Security Trust Fund could be about \$450 million.<sup>6</sup> This figure was calculated by multiplying the number of last-day cases reported in Texas and Georgia (4,819) by SSA data on average annual offset amount (\$4,800) and the average life expectancy upon receipt of spousal benefits (19.4 years). These estimated payments would likely increase as use of the exemption grows.

Options for addressing potential abuses of the GPO exemption include (1) changing the last day provision to a longer minimum time period or (2) using a proportional approach based on the number of working years as a government employee spent in covered and noncovered employment for determining the extent to which the GPO applies. The first option would require only small changes to administer and has precedent in 1987 legislation that required federal employees who transferred from the Civil Service Retirement System (CSRS) to the Federal Employees Retirement System (FERS) to remain in FERS for 5 years before retirement to be exempt from the GPO. The second option may represent a more calibrated approach to determining benefits for individuals who have made

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<sup>5</sup> Technically, individuals could have used this exemption since its passage in 1977. However, nearly all of the transfers we identified in Texas and Georgia occurred in the last several years.

<sup>6</sup> This estimate may over/under estimate costs due to the use of averages, the exclusion of inflation/cost-of-living/net present value adjustments, lost investment earnings by the Trust Funds, and other factors that may affect the receipt of spousal benefits.

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contributions to the Social Security system for an extended period of their working years. However, SSA has noted that a proportional approach would take time to design and would be administratively burdensome to implement, given the lack of complete and reliable data on noncovered Social Security employment.

The GPO “loophole” raises fairness and equity concerns for those receiving a Social Security pension and are currently subject to an offset of their spousal Social Security benefits. In the states we visited, individuals with a relatively small investment of work time and only minimal Social Security contributions can gain access to potentially many years of full Social Security spousal benefits by using the GPO exemption. Also, providing full spousal benefits to individuals who receive government pensions and made only nominal contributions to the Social Security system runs counter to the nation’s efforts to address the solvency and sustainability of the Social Security program. Finally, the last-day exemption could have a more significant impact if the practice grows and begins to be adopted by other states and localities.

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## Matter for Congressional Consideration

Considering the potential for abuse of the last-day exemption and the likelihood for its increased use, we believe timely action is needed. We are making a matter for congressional consideration that the last-day GPO exemption be revised to provide for a longer minimum time period. This action would provide an immediate “fix” to address possible abuses of the GPO exemption identified in our review.

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## Agency Comments

We provided a draft of this briefing to SSA officials for comment on July 3, 2002. On July 8, 2002, SSA provided oral comments on our draft briefing. SSA generally agreed with our briefing’s findings and provided several technical comments, which we incorporated where appropriate. We also provided a draft of this report to the Commissioner of Social Security for comment. On August 7, 2002, we obtained written comments on our draft report from SSA. SSA generally agreed with our report’s findings and provided several technical comments, which we incorporated where appropriate.

We are sending copies of this report to relevant congressional committees and other interested parties and will make copies available to others upon request. In addition, the report will be available at no charge on the GAO Web site at <http://www.gao.gov>.

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If you or your staff have any questions about this report, please contact me on (202) 512-7215 or Daniel Bertoni on (202) 512-5988. Patricia M. Bundy, Jamila L. Jones, Daniel A. Schwimer, Anthony J. Wysocki, and Jill D. Yost also made key contributions to this report.

Sincerely yours,

A handwritten signature in black ink, reading "Barbara D. Bovbjerg". The signature is fluid and cursive, with the first name "Barbara" written in a larger, more prominent script than the last name "Bovbjerg".

Barbara D. Bovbjerg  
Director, Education, Workforce,  
and Income Security Issues





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## **“Last Day of Employment Exemption” to the Government Pension Offset (GPO)**

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**Briefing for  
Committee on Ways and Means,  
Subcommittee on Social Security**

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## Overview

- Background
- Objectives
- Scope and Methodology
- Summary of Results
- Findings by Objective
- Concluding Observations
- Matter for Congressional Consideration



## Background: Social Security Coverage

- The Social Security Act requires that most workers be covered by Social Security retirement benefits. Workers contribute to the program via wage deductions. State and local government workers were originally excluded from Social Security because many were already covered by their state or local government's pension plan.
- Starting in the 1950s, state and local governments had the option of selecting Social Security coverage for their employees or maintaining noncovered pension plans. In 1983, state and local governments in the Social Security system were prohibited by law from opting out of it.
- There are about 2,300 separate state and local retirement plans nationwide. About one-third of the workers in these plans are not covered by Social Security. Social Security coverage for state and local government employees varies within states.



## Background: Government Pension Offset (GPO)

- Generally, Social Security benefits are payable to the spouses of retired, disabled, or deceased workers covered by Social Security.
- If both spouses worked in positions covered by Social Security, each may not receive both the benefits earned as a worker and the full spousal benefit; rather the worker receives the higher amount of the two.
- Until 1977, workers receiving pensions from government positions not covered by Social Security could receive their full pension benefit and their full Social Security spousal benefits, as if they were nonworking spouses. In 1977, legislation created a Government Pension Offset (GPO) to equalize the treatment of individuals covered by Social Security and those with noncovered government pensions. GPO prevented workers from receiving a full spousal benefit on top of a pension earned from noncovered government employment.

<sup>1</sup>Public Law 95-216, Section 334 (1977). Currently, the reduction in spousal benefits is two-thirds of the amount of their government pension.



## Background: GPO “Last Day of Employment” Exemption

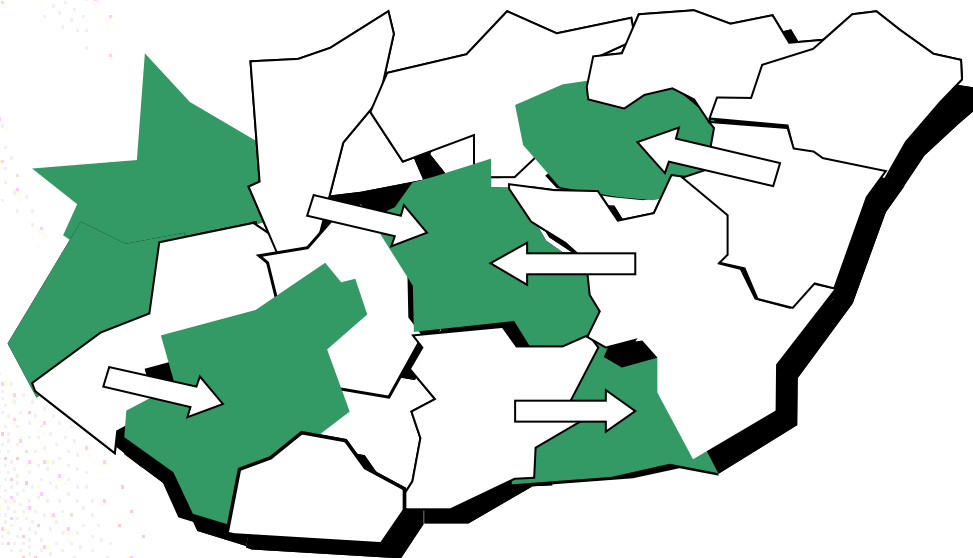
- The GPO does not apply if an individual’s last-day of state/local employment is in a position covered by both Social Security and the state/local government's pension system.<sup>2</sup>
  - Thus, individuals retiring from state/local government jobs not covered by Social Security may transfer briefly to another state/local government job covered by Social Security to avoid the GPO—provided that the subsequent job is covered by the same state/local government pension plan.
- The intent of the last-day exemption is unclear.

<sup>2</sup> Exemption due to “The Last Day of Employment” Covered Under Social Security – State/Local or Military Service Pensions (SSA’s Program Operations Manual System, GN 02608.102)



## Background: Hypothetical Example of Worker Transfers to Use Exemption

Worker Movement across Counties in State with Mixed Social Security Coverage



Note: Arrows represent movement of individuals who belong to a statewide retirement plan from non-Social Security-covered counties (not shaded) to covered counties (shaded) to use the last-day GPO exemption.



## Objectives

- Assess the extent to which individuals retiring from jobs not covered by Social Security may be transferring briefly to jobs covered by Social Security to avoid the government pension offset (GPO).
- Estimate the impact of such transfers on the Social Security Trust Fund.
- Identify options for addressing potential abuses of the last-day exemption.



## Scope and Methodology

- Review originated from a referral to GAO's FraudNET questioning a practice in Texas where individuals were switching to Social Security-covered positions for 1-day to avoid the GPO.<sup>3</sup>
- Reviewed GPO's legislative history, government reports, and SSA's policies and procedures on the administration of the GPO and the GPO exemption.
- There is no central data on use of the GPO exemption by individuals and time constraints did not permit in-depth audit work on the approximately 2,300 state and local retirement plans nationwide.
- Thus, to assess the extent of these job transfers we performed limited work with associations, researchers, and retirement system officials in 28 states. States selected either because they were authorized to operate retirement systems with both covered and noncovered positions or their state/local government plans had a mix of covered and noncovered positions, offering the greatest potential for use of the last-day exemption.
- Interviewed and obtained documentation from SSA headquarters and regional officials; and other federal officials such as the Congressional Budget Office and the Internal Revenue Service.
- Visited and performed audit work in Texas and Georgia, two of the states where we identified use of the last-day exemption.

<sup>3</sup> FraudNET is a service maintained by GAO's Office of Special Investigations. GAO determined that use of the GPO last-day exemption is permitted under the law.





## Summary of Results

- GPO exemption is used in two states, where use is growing.
  - Given our time constraints we could not definitively confirm that this practice is occurring in other states.
  - SSA does not track or maintain data on use of the GPO exemption.
  - Texas and Georgia officials reported 4,819 cases as of June 2002<sup>4</sup> (Texas—4,795; Georgia—24). However, officials in both states indicated use of the exemption would likely continue to grow as awareness of it increases.
  - SSA officials acknowledged that exemption use might be possible in some of the approximately 2,300 state and local government retirement plans in other states where such plans contain Social Security covered and noncovered positions. There is little awareness of the exemption among state/local pension plan administrators and experts in the public pension field.
  - Retirement plan officials in other states we contacted noted their plans may permit use of exemption because of the structure of their plans, but did not report actual cases.
- Cases in Texas and Georgia could result in increased long-term benefit payments from the Trust Fund of about \$450 million.
  - Texas accounted for about 99.5 percent of this estimate; Georgia about 0.5 percent.
  - Transfers reported by Texas and Georgia officials in 2002 accounted for most of this amount (many schools began only recently to offer such work, and did not maintain complete records for prior years).
  - Estimated long-term impact likely to grow as use of the exemption grows.
  - Cost estimates may over/under estimate costs due to the use of averages, the exclusion of inflation/cost-of-living/net present value adjustments, and other factors that may affect the receipt of spousal benefits.
- Options to address potential abuses.
  - Change the last-day provision to a longer minimum time period.
  - Use a proportional approach to determine whether GPO applies.

<sup>4</sup> Technically, individuals could have used this exemption since its passage in 1977. However, nearly all of the transfers we identified in Texas and Georgia occurred in the last several years.



## Extent of Transfers to Avoid the GPO: Texas Summary

- Officials reported that 4,795 individuals at 31 schools have used or plan to use last-day employment to take advantage of the GPO exemption.
  - In 2002, one fourth (3,521) of all Texas public education retirees took advantage of this exemption.
- According to information from school officials and associations, use of the exemption has increased since 1990 (the earliest use reported to us).
  - For example, officials in one school district reported rapid growth—from one worker in 1996 to 1,050 in 2002.
  - A school district that began offering last-day employment this year has received over 1,400 applications from individuals seeking to use the exemption.



## Extent of Transfers to Avoid the GPO: Texas Summary

- According to school officials and our analysis of exemption use and trends in Texas teacher retirements, use of the exemption is likely to grow further.
  - Retirements have increased in past years and are likely to grow further (about 14,000 in 2002; up from 12,000 in 2001, and 10,000 in 2000).
  - Availability/use of the exemption is being publicized by teaching associations and groups (Web sites, newspapers, seminars, etc.) and by word-of-mouth. For example, one website we identified lists the names and telephone numbers of school officials in counties covered by Social Security and how to contact those officials for such work.
  - Use of the exemption is becoming part of individuals' retirement planning. For example, at one university we visited, officials are scheduling work days for imminent retirees through 2005.
  - Individuals are willing to travel to take these jobs. Officials in one school district noted that a teacher traveled 800 miles to use the last-day provision.



## Extent of Transfers to Avoid the GPO: Texas Summary

- Teachers worked under a variety of arrangements to use the GPO exemption:
  - In most schools, employees typically work a single day in a job covered by Social Security.
  - Nearly all positions reported by officials were non-teaching jobs, including clerical, food service, or maintenance.
  - Most of these employees are paid about \$6 per hour. At this rate, the Social Security taxes deducted from their pay would total about \$3.
  - Some schools charge a processing fee (ranging from \$100-\$500) to hire these workers. Fees are a significant source of revenue—this year one school district collected over \$283,000 in fees.



## Extent of Transfers to Avoid the GPO: Excerpts from Texas Web sites

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Excerpt about the GPO exemption on a teaching association's Web site:

"[We have] received many inquiries about the loophole that allows some school employees to receive the full amount of both their TRS pension and their Social Security benefit. Most Texas school employees do not participate in Social Security, so according to federal law, the amount of any Social Security benefit to which they are entitled is reduced or eliminated by the amount of their TRS benefit. ... [We have] become aware of some school districts that participate in both TRS and Social Security facilitating the use of this loophole by agreeing to hire employees for one day to allow the employee to become exempt from the Social Security offset. A list of Texas school districts participating in Social Security is available on [our] website."

Excerpt about the GPO exemption on a retirement/financial planning Web site:

"You may be eligible to receive both teacher retirement and social security benefits even if you have never worked a day under social security. As little as one day of work in a dual system (Teacher Retirement System *and* Social Security System) will give you half of your spouse's social security benefits when you reach retirement age. When you reach retirement, you will receive 1/2 of your spouse's benefit and/or the widow(er) benefit for the rest of your life. This could mean \$150,000 or more in benefits throughout your lifetime. Not too bad for as little as one day of work under a dual system!"

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## Extent of Transfers to Avoid the GPO: Georgia Summary

- Officials in one district reported that 24 individuals have used or plan to use employment to take advantage of the GPO exemption.
- Officials expect use of the exemption to increase as awareness of it grows.
- Teachers typically transfer to another teaching position for about one year in a school district covered by Social Security.



## Extent of Transfers to Avoid the GPO: Georgia Summary

- Our review and analysis of information provided by officials indicate that the environment is conducive to such transfers.
  - A teacher shortage outweighs the risk of teachers leaving after one year. Fast-growing school systems reported they needed to hire teachers even if they only intended to teach for one year.
  - Some schools have had teachers leave shortly after being hired. For example, in one district, a teacher signed a one-year contract to teach but left after 61 days.
  - In some school employment applications we reviewed, individuals explicitly stated their desire to work in a county covered by Social Security to obtain full Social Security spousal benefits.



## Extent of Transfers to Avoid the GPO: Where Exemption Could Be Used

- According to state/local retirement plan officials in other states, transfers to avoid the GPO are possible because the structure of their plans allows covered and noncovered Social Security positions. Officials did not report any actual cases, however.
  - In a midwestern state with a retirement plan for all state government employees, it is possible for law enforcement personnel (noncovered) to take a covered job in the state insurance bureau (covered) just before retiring to avoid the GPO.
  - In a southern state with a statewide retirement plan for school employees, teachers and other school professionals (noncovered), can potentially transfer to a job in the school cafeteria (covered) to avoid the GPO.
  - In a north central state, a retirement system official reported hearing of a few cases where teachers had taken advantage of the exemption by transferring to jobs in other school districts covered by Social Security.
  - In a western state with a statewide retirement plan, workers could move from a noncovered position in a government agency to a covered position in another agency to use the GPO exemption.
- SSA officials acknowledged that exemption use might be possible in some of the approximately 2,300 state and local government retirement plans in other states where such plans contain Social Security covered and noncovered positions.
- SSA does not maintain data with respect to last-day transfers in noncovered retirement plans. Time constraints did not permit us to review the approximately 2,300 state/local retirement plans to assess the extent of use of the last-day exemption.





## Impact of Employee Transfers on Social Security Trust Fund

- The individuals reported to have used the exemption by Texas and Georgia officials could result in increased long-term benefit payments from the Trust Fund of about \$450 million.
  - Calculated by multiplying the number of last-day cases reported by Texas and Georgia officials (4,819) by SSA data on average annual offset (\$4,800) and life expectancy upon receipt of spousal benefits (19.4 years). Estimates may over/under estimate costs due to the use of averages, the exclusion of inflation/cost-of-living/net present value adjustments, lost investment earnings by the Trust Funds, and other factors that may affect the receipt of spousal benefits.
- Estimated potential long-term fiscal impact varied by state.
  - Texas – 4,795 cases accounted for about 99.5 percent of our estimate.
  - Georgia – 24 cases accounted for about 0.5 percent of our estimate.
- Employee transfers reported in 2002 accounted for most of this amount.
  - Many schools officials told us that they did not maintain complete records for prior years and/or began only recently to offer such work.
- Fiscal impact may increase over time if use of the exemption becomes more institutionalized.



## Options for Addressing Potential Abuses

- Change GPO last-day exemption provision to a longer minimum time period.
  - For example, 1987 legislation required that federal employees who transferred from the Civil Service Retirement System (CSRS) to the Federal Employees Retirement System (FERS) must remain in FERS for 5 years before retirement to be exempt from the GPO.
  - We found that most of the jobs in Texas last for about one day, so extending the time period might eliminate many of the exemption users in Texas.
  - The use of a longer minimum time period would be less burdensome than other methods for SSA to administer.
- Use a proportional approach for determining the extent to which the GPO applies.
  - For example, employees who have spent a certain proportion of their working career as a government employee in a position covered by Social Security could be exempt from the GPO.
  - On the whole, this might be a more calibrated approach to determining benefits for individuals who have made contributions to the Social Security system for an extended period of their working years.
  - SSA has noted that using a proportional approach would take time to design and would be administratively burdensome to implement, given the lack of complete and reliable data on noncovered Social Security employment.



## Concluding Observations

- The GPO “loophole” raises fairness and equity concerns.
  - Individuals receiving government pensions can potentially receive full spousal Social Security benefits for their retirement lifetime, while those receiving a Social Security pension and a spousal benefit will have the spousal benefit reduced.
- Based on the number of people reported to be using the loophole in Texas and Georgia this year, the Trust Fund liability is increasing by hundreds of millions of dollars, a figure which could grow more in coming years.
  - Although the fiscal impact we identified represents a relatively small percentage of the Social Security Trust Fund, these costs could increase significantly if the practice grows and begins to be adopted by other states and localities.
  - Use of the loophole has grown in localities we visited and increasing awareness is making it part of individuals’ retirement planning.
  - Our analysis suggests that use of the exemption may grow further as the aging baby-boom generation begins to retire in large numbers.
- The GPO loophole runs counter to the nation’s efforts to address the solvency and sustainability of the Social Security program.
  - Thus, the exemption appears to provide a loophole for only a select group of individuals, awarding benefits to workers who have paid very little to Social Security and already receive public pension benefits.



## Matter for Congressional Consideration

- To address potential abuses of the GPO's last-day exemption, the Congress should consider revising the Social Security Act to extend the last-day provision to provide for a longer minimum time period.
  - This revision would be consistent with 1987 legislation that addressed the GPO exemption's applicability to federal employees under the Federal Employees Retirement System and the Civil Service Retirement System.
  - Timely action would provide an immediate "fix" to possible abuses of the GPO exemption.

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